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PASS TO OPIC (JIM WILLIAMS)

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SUBJECT: PRC Engagement in the DRC

REF: A. STATE 41697
¶B. 06 KINSHASA 1731
¶C. 07 KINSHASA 1133
¶D. KINSHASA 406

¶1. (SBU) Summary: The story of Chinese (PRC) involvement in the Democratic Republic of Congo (DRC), dating to the 1970's when the DRC was barely into its second decade as an independent nation, is long and complex. Since the early 2000's, China has ramped up its presence and exchanges with the DRC, mostly on the basis of trade in the Congo's natural resource sector. What was earlier an informal, somewhat disorganized collection of Chinese businesses, most operating in the Katanga Province of southern DRC, has begun to be formalized over the past year, beginning with a large, multi-billion dollar agreement between three large Chinese parastatals and the GDRC, signed in September 2007. In early 2008 some of the agreement's details were made public and it was confirmed that this is an exchange of millions of tons of copper and cobalt for infrastructure projects, to be carried out by Chinese firms. Many other Chinese investments and projects are being considered or are already in the works, including road building, hydroelectric installations, a deepwater port, and huge bio-diesel plantations. There are obvious benefits and drawbacks to all of these activities, but it is difficult at this time, due mainly to the lack of transparency surrounding these potential deals, to determine whether the results for the DRC will be net positive or negative. There is little or no coordination/cooperation between the U.S. and China missions in the DRC, and future bilateral actions will need to be examined on a case-by-case, sector-by-sector basis. End summary.

The DRC: A History of Chinese Involvement

¶2. (SBU) This is a response to STATE 41697 (ref A). Chinese involvement in the DRC dates to the Mobutu era (1965-97), when large, highly visible projects were the rule. The Stade des Martyrs (Martyrs Stadium) project (which is now in such disrepair that FIFA refused to schedule soccer games there unless the DRC made repairs to the tune of USD three million by end April 2008; this was not achieved), the Palais du Peuple (the Parliament Building) and other infrastructural projects including hospitals were all completed during the 1970's, 1980's, and early 1990's. Following the economic collapse of the early 1990's and the subsequent conflicts that have wracked the Congo, Chinese presence was less visible and funding seemed to dry up. All this has changed now that the DRC is emerging from over a decade of war and worldwide demand for commodities, especially metals including copper and cobalt, has skyrocketed along with the prices for those metals. The DRC and China signed a declaration establishing a "strategic partnership" during the Beijing Summit Forum on China-Africa Cooperation in November 2006.

Even before this signing, the state-owned China National Overseas Engineering Company (COVEC) loaned the DRC copper and cobalt mining parastatal, GECAMINES, USD 60 million to reopen a copper mine in Katanga Province. At about the same time, the Chinese government loaned the GDRC USD 32 million to fund a mobile phone network in support of the Congo China Telecom company, a cellular service provider (ref B).

China/DRC Trade: Growing by Leaps and Bounds

¶3. (SBU) DRC exports to China doubled between 2003 and 2004, while Congolese imports from China increased by more than 50 percent in each of the three years following the establishment of a transitional government in 2003. 2007 saw sustained levels of exports, mostly mineral ores, that attained nearly USD three billion for the year. Imports from China nearly doubled between 2006 and 2007 to over USD four billion, meaning that a country with a budget of barely more than USD two billion had a nearly USD one billion trade surplus with China. Preliminary figures for 2008 show no decline in this trend, with January figures indicating a nearly 50 percent increase in exports to China and a nearly 100 percent increase in imports from China over the same month in 2007. At this rate, the DRC may post a USD three billion trade surplus with China alone, rivaling the level of the national budget for the year. As in the days of King Leopold (1876 - 1909), much of the Congo's natural resource wealth is leaving the country, while the population still has relatively little purchasing power to buy the products, even cheap ones, that it needs or wants.

Initially Small, Scattered Mining Operations

¶4. (SBU) Much of the Chinese business in the DRC was, until recently, of an informal and ad-hoc nature. In the copper belt area of the DRC's Katanga Province, small Chinese-owned operations bought copper and cobalt ore that had been scraped together virtually by hand and concentrated to the extent possible before being shipped in "big bags," flexible sacks with a handle capable of holding around one ton each and transported on trucks carrying 20 of them at a time to ports in Dar es Salaam or Durban for onward shipment to China. China, although it has significant reserves of cobalt itself, became the world's leading producer of cobalt metal, much of it sourced from Katangan mines that were being picked over by thousands of Congolese artisanal miners, some of them underage and all of them poorly equipped, working in dangerous conditions and earning a pittance. (Note: The DRC is estimated to have about a third of the world's known cobalt reserves. End note.)

Katumbi Lowers the Boom

¶5. (SBU) Much of this trade came to an abrupt halt in early 2007 following the elections of late 2006, when the new governor of Katanga Province, Moise Katumbi, decreed that all exports of raw, concentrated but unprocessed ores were prohibited. This edict put a temporary halt to most of the illegal, and even some of the legal, exports of copper and cobalt ore that had been occurring unchecked since the early 2000s. Total Chinese exports from the DRC dropped by more than a quarter during the first half of 2007, and did not begin to recover their previous level until midway through the year.

China Steps up with Larger Projects, More Money
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¶6. (SBU) Coincidentally, official Chinese investment in the DRC, with an eye toward regaining the metal ore exports needed to support the booming Chinese economy, began in earnest in mid-2007. In August 2007, a delegation of Chinese businesses, including the ExIm Bank of China, the China Railway Engineering Corporation (CREC), and SINOHYDRO signed an agreement ("protocole d'accord") with the Congolese Minister of Infrastructure, Public Works and Reconstruction, Pierre Lumbi. The agreement makes reference to

cooperation agreements dating to 2001, during a period when the DRC was perhaps at its lowest ebb. The agreement is seven pages long and includes two annexes that lay out the modalities of payment for infrastructural projects to be completed by Chinese companies, basically a swap of over eight million tons of copper, over 200,000 tons of cobalt, and 372.3 tons of gold (source "to be found") worth USD 3 billion for a package of railway, roads and buildings (hospitals, health centers, universities and houses) estimated to cost over USD six billion dollars.

Details of the Agreement

¶7. (SBU) A joint venture company, 32 percent Congolese and 68 percent Chinese, would be financed by the output of the mining concessions specified in the agreement, most of them, except for the gold mines, located in Katanga Province. The agreement gives the joint venture company all standard investment advantages set by the DRC investment and mining codes, as well as a nearly complete exoneration of taxes, duties and customs on all imports and exports. The company is free to name its suppliers and to hire whomever they choose "both inside and outside the country." All DRC dividends from the company are to be used to pay back the initial costs, unless they are paid off "in-kind," (i.e. by more natural resources.) The term of the agreement is 30 years. The agreement was signed on September 17, 2007 (ref C), and included an additional USD two billion for additional China-DRC joint ventures in the mining sector. A virtually identical deal was signed in October with the China Development Bank.

¶8. (SBU) Paul Fortin, the expatriate head of DRC state copper and cobalt mining parastatal, GECAMINES, spent over a month in China at the end of 2007 negotiating some of the fine print. In January, it was announced that a deal had been signed and that the joint venture company, SICOMINES, would be backed by rights to two mining concessions with estimated reserves of 10 million tons of copper and 2 million tons of cobalt. At current market prices, these reserves are worth approximately USD 83 billion and USD 435 billion, respectively. One estimate is that ultimately the Chinese will earn

a profit of over USD 40 billion after the initial investment is paid back. As of April 2008, there is little to show from this agreement as details continue to be ironed out. An announcement in mid-April stated that USD 700 million would be released this year to fund some of the infrastructural projects listed in the agreement. One is the construction, or re-construction since the road already exists, of the 60 miles of highway between Lubumbashi, the capital city of Katanga Province, and Kasumbalesa, the major land border crossing between the DRC and Zambia. This is not only the largest import/export crossing point in the DRC after the Matadi Port, which supplies the megalopolis of Kinshasa; it is also the point through which the vast bulk of the copper and cobalt due to be produced eventually will have to pass.

And That's Not All...

¶9. (SBU) There are other Chinese investments and projects in the works and being proposed. The China National Machinery, Equipment and Export Corporation (CEMEC) has already agreed to a USD 75 million loan for chrome and nickel mine in the Kasai provinces of central DRC, not far from the provincial capitals of Kananga and Mbuji Mayi (ref B). Kasai Occidental and its neighbor to the east, Kasai Oriental, site of the state diamond mining parastatal, MIBA, are isolated and underserved partly due to the decrepit condition of the rail line that passes through them from the Congo River north and west of the Kasais, down to the copper belt south and east of them. What was once daily service bringing goods both down from Kinshasa and up from Lubumbashi is now a maybe once-a-week train that makes irregular deliveries of basic good such as fuel and corn meal that can cost twice as much as in the rest of the country, when available. Despite the fact that the highly touted Inga-Shaba line, which delivers power from the Inga hydroelectric installations of Bas Congo to the mines of Katanga Province and points south (Zambia, Zimbabwe and South Africa), the Kasais are virtually without power

other than local generators since the transmission line was never branched for them. (See ref D for more information on the Inga hydroelectricity project).

¶10. (SBU) China has expressed interest in possibly expanding Inga and working with the MIBA diamond mines. It has even floated the possibility of creating a deepwater port at Banana, the DRC's Atlantic Ocean port that currently cannot handle the large, ocean-going cargo ships that dock at Pointe Noire, a few hundred miles up the coast in the Republic of the Congo. During the January 2008 visit of Chinese Foreign Minister Yang to the DRC, Yang announced a preferential loan agreement worth USD 33.6 million, financed by the ExIm Bank of China, to create a fiber optic trunk in the DRC, built by the China International Telecommunication Construction Corporation.

Fuel for China: Bio-Diesel, Oil, and Uranium?

¶11. (SBU) It has been widely reported, though unsubstantiated, that a Chinese company, ZTE International, is considering investing USD one billion in order to create a three million hectares (11,500 square miles, an area the size of a square with 100 mile-long sides) of oil palm plantations in the Equateur, Bandundu, Orientale and Kasai Occidental provinces to produce bio-diesel. (Note: The DRC has millions of hectares of existing oil palm plantations dating back to pre-independence days, but many of them are no longer producing due to age and lack of maintenance. End note.) China has shown little interest in DRC petroleum since its production (25,000 barrels/day) pales in comparison (well less than 10 percent) with that of Nigeria, Angola, Sudan, Equatorial Guinea, Gabon and the Republic of the Congo, but this could increase as more western companies begin onshore exploration here. Finally, it is well-known that China is interested in uranium for its nuclear plants and that someday the DRC may open up its uranium mines again. (Note: Uranium mining in the DRC is currently prohibited by a President Kabila decree, occasioned by earlier security concerns and lack of effective border control. End note.)

The "Pros" of Chinese Engagement

¶12. (SBU) Official, above-board Chinese investment and activity in the DRC directly addresses the country's most urgent needs, as expressed by President Kabila in his 2006 inaugural address, better known as the "Cinq Chantiers" (five pillars of reconstruction) speech: infrastructure; employment creation; housing, water and

electricity; health; and education. While the details are still fuzzy in some cases, and the numbers may be off a bit, we do know that some 2000 miles of railway linking Katanga and Bas Congo provinces, 2000 miles of roadway linking Orientale and Katanga provinces, 31 hospitals, 145 health centers, two large universities and 5,000 government housing units are pledged. A Chinese company is already working on the Matadi to Kinshasa road, ironically under a World Bank funded program. Another Chinese company is next door to the DRC already, rehabilitating the Benguela, Angola to Dilolo, DRC rail line that will open up an alternate route westward to the Atlantic Ocean for Congolese mining exports.

¶13. (SBU) In each of the China-DRC joint ventures revealed during the past year, much of the attention is paid to the infrastructure and job creation necessitated by the project rather than the actual outputs (e.g. chrome and nickel in the Kasais.) Reliable water and electricity for processing plants, adequate roads to handle incoming equipment/materials and outgoing production, and upgraded health, education and housing for workers and their families are all right out of the "cinq chantiers" playbook. (Note: this type of cradle-to-grave coverage of employees, especially in the Katanga Province copperbelt, was the norm for tens of thousands of employees of Congolese companies such as GECAMINES. End note.)

The "Cons" of Chinese Engagement

¶14. (SBU) Based upon past experience and from observing current Chinese business practices in neighboring countries (Angola and Zambia in particular), the DRC is likely aware of the obvious negatives: less local job creation and procurement than expected, less cost-savings than promised, and poorer quality (and dependability) of the infrastructure left behind. The DRC may perhaps be unaware of, or not care about, other more subtle drawbacks. These include the opening up of areas through road building that may increase illegal logging, exacerbate destruction of rainforest habitat, and provide opportunities for unscrupulous bushmeat hunters. Certainly the idea of creating entirely new plantations by first cutting down existing forest cover should give the GDRC authorities pause. Surprisingly, GDRC authorities appear to have overlooked the fact that they were in the midst of a controversial mining contract review of over 60 joint venture deals dating back to the late 90s when they signed the September agreement with the Chinese. It was the DRC's inability to know for sure what they were giving away in those contracts, and then finding out that they had made bad deals, that necessitated the review. This time, perhaps, the participation of GECAMINES CEO Paul Fortin has assuaged those fears.

Formal IMF Program Imperiled by Chinese Loans

¶15. (SBU) The IMF has been told by GDRC authorities that the DRC 2008 budget of USD 3.4 billion includes a USD 250 million "signing bonus" of unearmarked Chinese funding that will be paid to the GDRC sometime in the second half of 2008. IMF officials, unconvinced of the supposed "concessional" nature of some of these billions of dollars of Chinese loans, are asking that the terms of the loans be made known, and renegotiated if necessary, in order to requalify the DRC for a new Poverty Reduction and Growth Facility program (PRGF). Without this new PRGF, the DRC will not be able to achieve the debt forgiveness, estimated at over USD 10 billion, that it so desperately needs from the Paris Club through the Heavily Indebted Poor Country (HIPC) initiative. If the DRC can address IMF concerns, get the quarter million dollars from the Chinese, renegotiate a PRGF and achieve HIPC completion point before end 2008, it will have avoided, perhaps, the biggest potential negative of this latest Chinese engagement in the DRC.

¶16. (SBU) Comment. Other than the IMF issue regarding the concessionality of the Chinese loans, it is difficult to predict whether the DRC stands to ultimately win or lose from its dealings with China. If much-needed infrastructure projects begin soon and provide some local employment and contracts for Congolese suppliers, nobody would claim that this was a bad thing. President Kabila has been in office for nearly a year and a half, with not much to show in the way of progress on his "cinq chantiers." As with the two Inga hydroelectric plants and plans for an Inga III and possibly a "Grand Inga" project, the costs of just rehabilitating existing infrastructure in the DRC, no less building new, are staggering and beyond the means of any one bilateral or multilateral donor. At present, there is virtually no contact between the U.S. and China

missions in the DRC, although China has apparently decided to at least attend some of the donors' group meetings held in Kinshasa. Any bilateral cooperation or coordination with the Chinese in the DRC would best be done on either a case-by-case or a sector-by-sector basis. End comment.

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